



## MEMORANDUM

TO: CollegeCounts, Alabama 529 Savings Program DATE: January 25, 2012

FROM: Pension Consulting Alliance, Inc. (PCA)

cc: Jeremy Thiessen – PCA  
Eric White – PCA  
Andrea Feirstein – AKF

RE: **CollegeCounts “Watch” Status Update**

### Summary

PCA has reviewed the CollegeCounts Direct and Advisor Plan data as of December 31, 2011. Currently, only the Harbor Large Cap Value Fund (Advisor Plan) remains on “Watch” status. At the end of the period, two new funds qualify for “Watch” status under the Monitoring Procedures and Criteria. PCA is recommending “Watch” status for the Fidelity Advisor Mid Cap II Fund (Direct and Advisor) and the BlackRock Inflation Protected Bond Fund (Advisor) at this time for performance reasons. PCA also recommends an additional 3-6 months to monitor the Harbor Large Cap Value Fund (Advisor) as performance has improved over the last 12-months, however, the improvement does not yet warrant removal of “Watch” status. Each of these items is discussed in more detail below.

### Discussion

#### Funds Currently on “Watch” Status

As of December 31, 2011, only one fund remains on “Watch” status. The Harbor Large Cap Value Fund (Advisor Program) was placed on “Watch” by the Board at the February 2011 meeting for performance reasons based on data as of 12/31/2010.

#### **Performance of Funds on Watch Status As of 12/31/2011**

Funds on Watch Status	Program	Board Action Date	Watch Status Start Date	No. Months Since Watch Began	Excess Performance			
					3 Mo.	6 Mo.	9 Mo.	Since Watch
Harbor Large Cap Value	Advisor	2/9/2011	1/1/2011	12	-1.0%	-0.1%	1.6%	-0.3%

Since being placed on “Watch” status, the fund has underperformed its benchmark by (30) basis points, despite a robust performance period during the initial 9-months on “Watch” where the fund outperformed its benchmark by 1.6%. Underperformance since that time was due in part to poor relative performance in October and November 2011. Results at the end of the period show significant improvement and are within the acceptable range; however, it is not strong enough to warrant removal from “Watch” status. **PCA recommends Harbor remain on**

***“Watch” status for an additional 3-6 months until this improved performance trend is confirmed.***

**New Funds Qualifying for “Watch” Status**

PCA has conducted a review of the underlying funds in the CollegeCounts Direct and Advisor Sold College Savings Plans and have determined that, as of December 31, 2011, two additional funds qualified for “Watch” status under the Monitoring Procedures and Criteria approved by the CollegeCounts Board. PCA found that two funds, the Fidelity Advisor Mid Cap II and the BlackRock Inflation Protected Bond Funds, failed the short-term criteria established for “Watch” status. Each fund is discussed in more detail below.

Portfolios	On Watch	Criteria Utilized for Watch Status		
		Short-term	Medium-term	Long-term
Fidelity Advisor Mid Cap II	No	✓	N/A	N/A
BlackRock Infl Protected Bond	No	✓	N/A	N/A

N/A Watch status not applicable for time period due to fund inception date

✓ Indicates eligible for watch status as a result of performance

**Fidelity Advisor Mid Cap II (Direct and Advisor Plan)**

The Fidelity Advisor Mid Cap II Fund currently falls below Criteria #2 (Short-Term Performance Criteria) with a rolling 12-month excess performance below -2.75% for six consecutive months. The Portfolio has historically been a strong performer. However, the fund exhibits a growth bias which has created a cyclical relative performance pattern as growth stocks/sectors go in and out of favor. This cyclical performance should be expected and does not denote any lack of ability on behalf of the fund manager’s ability to add value. However, near term performance has been exceedingly difficult for the fund as it ended the year trailing its benchmark by over 8%. Aside from the fund’s style bias, this near term underperformance can also be attributed to its large weighting to international stocks, which performed poorly over the past year. ***PCA recommends the Fidelity Advisor Mid Cap II Fund be placed on “Watch” status and closely monitored over the next 12 to 18 months.***

**BlackRock Inflation Protected Bond (Advisor Plan)**

The BlackRock Inflation Protected Bond Fund currently falls below Criteria #2 (Short-Term Performance Criteria) with a rolling 12-month excess performance below -0.75% for six consecutive months. The Portfolio has historically generated steady performance and has consistently been managed more conservatively than its peers and, often times, its benchmark. This cautious approach paid dividends during the credit crisis and other instances of market turbulence as its conservatism has led the portfolio manager to hold up to 10% cash and shorten the duration relative to the benchmark. However, this positioning is the cause of the near term underperformance as longer duration bonds outperformed over the past year. It is likely that the fund’s conservative approach may pay dividends again in the future if interest rates start to rise from current historic lows. ***PCA recommends the BlackRock Inflation Protected Bond Fund be placed on “Watch” status and closely monitored over the next 12 to 18 months.***